



0000096679

ORIGINAL EXCEPTION

BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

WILLIAM A. MUNDELL

Chairman

JIM IRVIN

Commissioner

MARC SPITZER

Commissioner

DOCKETED

MAR 21 2002

RECEIVED

2002 MAR 21 A 11:50

AZ CORP COMMISSION
DOCUMENT CONTROL

DOCKETED BY

nae

IN THE MATTER OF THE GENERIC
INVESTIGATION INTO U S WEST
COMMUNICATIONS, INC.'S COMPLIANCE
WITH CERTAIN WHOLESALE PRICING
REQUIREMENTS FOR UNBUNDLED
NETWORK ELEMENTS AND RESALE
DISCOUNTS.

DOCKET NO. T-00000A-00-0194
PHASE II

**QWEST CORPORATION'S EXCEPTIONS TO ALJS' MARCH 8
SUPPLEMENT TO THE RECOMMENDED OPINION AND ORDER**

Qwest Corporation respectfully submits these exceptions to the March 8, 2002
Supplement to the ALJs' November 8, 2001 Recommended Opinion and Order.

SUMMARY

No one disputes that the "essential objective" of TELRIC "is to determine what it would
cost, in *today's* market, to replace the functions of [a network] asset that make it useful,"¹ while
taking as given real-world constraints external to the network. *See* Qwest Exc. 10-11, 33-34.

The consensus on that issue is unsurprising, because those are the FCC's own words.

The ALJs nonetheless continue to violate this standard, most recently in their March 8
supplemental recommendation, which is designed to address issues left unresolved in the ALJs'

¹ Br. for Petitioners FCC and United States, *Verizon Communications Inc. v. FCC*, No. 00-511
and consolidated cases, at 6 (filed April 2001) ("FCC 2001 S. Ct. Br.") (emphasis added).

principal November 8 recommendation. Indeed, the ALJs simply ignore Qwest's position on several of the most important issues in this proceeding, such as nonrecurring charges, high capacity loops, collocation materials, and four-wire loops. That is not reasoned decision making. If adopted in anything like its present form, the ALJs' recommended order would not only violate TELRIC, but also undermine the incentives of Qwest and CLECs alike to invest in new telecommunications facilities for Arizona. For a fuller explanation of the ways in which skewing the TELRIC inquiry can foreclose the possibility of facilities based competition, please see the Statement of Harry M. Shooshan, attached to these exceptions as Exhibit A.

ARGUMENT

Qwest's principal exceptions are set forth in its December 12 filing, and Qwest limits its further exceptions here to the Supplemental RO&O. To keep this proceeding focused, Qwest has confined its challenges to the most straightforward and consequential of the ALJs' errors.

I. Nonrecurring Charges.

The Supplemental RO&O does not acknowledge, let alone respond to, Qwest's principal objections to the CLEC cost model for nonrecurring charges ("NRCs"). Qwest respectfully refers the Commission to its previous exceptions-phase briefs, which discuss the flaws of that model at some length. Given the importance of these charges, however, and given the ALJs' disquieting confirmation that they did indeed mean to recommend the CLEC model for *all* nonrecurring charges, Qwest briefly summarizes the most glaring respects in which that model would deny meaningful compensation for highly labor-intensive tasks.

To install a DS0 loop (a "basic installation"), any efficient provider's personnel must process the order, schedule the workload, go to the central office distribution frame, identify the relevant facilities, disconnect the correct loop from the switch port, run jumper cables to the

CLEC's collocation facilities, and notify the CLEC that the job has been completed. *See* Qwest Exc. 38-40. In their November 8 recommendation, the ALJs proposed a one-time \$1.70 charge to cover all of those labor-intensive activities, even though \$1.70 would not cover even the cost of gas and mileage for a network technician's trip to the central office. In their post-November 8 advocacy before the ALJs, the parties thus focused on two remaining questions. *First*, did the ALJs mean to apply that \$1.70 charge to cover not just non-coordinated loop cutovers, but also "coordinated installations" ("hot cuts") of DS0 loops?² *Second*, if so, did the ALJs also mean to apply that same \$1.70 charge to the total service Qwest provides when a CLEC instructs Qwest not just to perform the hot cut itself at the frame, but also to send technicians to the customer premises to conduct a battery of sophisticated tests on the line ("coordinated installation with test") – a service for which, in this very proceeding, Staff recommended a charge of \$141.67?³

Curiously, the ALJs' March 8 recommendation avoids any explicit discussion of any DS0 nonrecurring charge, even though DS0 hot cuts (with and without testing) are among the most frequently incurred non-recurring costs, and even though they were the principal focus of the parties' post-November 8 advocacy about nonrecurring costs. *See* Supp. RO&O at 8-9. That

² As explained in Qwest's prior submissions, a "hot cut" is a one-time service that a residential or business customer typically orders when it is already using a loop to receive service from Qwest and needs to avoid any lengthy interruption in service when Qwest technicians disconnect the loop from Qwest's switch and reroute it to the CLEC's network. To avoid such an interruption, Qwest and CLEC technicians must closely coordinate a number of labor-intensive tasks necessary to synchronize an efficient loop cutover, and the Qwest technicians must then stand by to resolve any reports of trouble on the line. *See* Qwest Exc. 42-43.

³ To conduct that test, these technicians visit the feeder-distribution interface and the customer premises to locate the proper connection points for the loop, verify that the loop is attached to the correct number in the central office, place a device on the line to check for shorts, verify dB losses, and then wait for confirmation from CLEC personnel that the loop actually works for its intended use. *See* Qwest Resp. to Exc. 12.

omission simply underscores the absence of any conceivable way to articulate how a nominal \$1.70 charge can be expected to cover the labor-intensive tasks necessary for basic DS0 loop installations, much less for coordinated DS0 loop installations, with or without testing.

AT&T's meaningless generalities about presumed cost savings "in a forward-looking environment" are no substitute for proof. As an initial matter, there is no dispute that, when Qwest performs even an *uncoordinated* ("basic") loop installation, it *must* make substantial use of human labor for both ordering and provisioning. AT&T suggests instead, however, that forward-looking technologies – which AT&T confuses with *future* technologies (*i.e.*, those that are not used today because they do not exist – *see* Tr. 1566) – will somehow enable carriers to avoid all such labor costs. That is nonsense.⁴ With respect to ordering, no carrier has achieved anything approaching the absurd 98% flow-through level AT&T posits here. That is both because the technology for that does not exist (as the CLECs' witness conceded), and because even if it did exist, many CLEC orders are either faxed or erroneous. *See* Qwest Exc. 35-38; Tr. at 1510-11, 1566-68 (Weiss Cross); Ex. Qwest-18 (Million Rebut.) at 47-48.

There is even less merit to AT&T's position on the nonrecurring costs of *provisioning* a loop. AT&T hypothesizes a world in which carriers purchase and install sprawling new fiber facilities and costly pre-switch electronics throughout their central offices to connect their own distribution frames directly to each other carrier's collocated facilities. *See* Qwest Resp. to Exc.

⁴ Customers do not and will not get service if one assumes that service just happens without any costs being incurred. In fact, a byproduct of setting costs at TELRIC levels is to ensure service continues to happen at levels consistent with the Commission's expectations. The Commission needs to set costs at a level that covers cost and allows the business to continue to function. Pretending costs "go away" or "just don't exist" benefits nobody: not customers, not the CLECs and not Qwest.

9-10. It is undisputed, however, that the technology for this bizarre arrangement is not “currently available,” 47 C.F.R. § 51.505(b)(1); *see also* Tr. at 1511, 1566 (Weiss Cross), and it is therefore irrelevant to a TELRIC inquiry. Just as important, even if such technology *were* currently available, the costs of all of the hypothesized fiber and electronics would be prohibitive, and those costs would of course need to be incorporated into the recurring cost model.

Needless to say, those prohibitive costs are *not* reflected in the ALJ-adopted CLEC model for either recurring or non-recurring costs, and neither the parties nor the ALJs have even tried to substantiate any suggestion that the recommended rates somehow cover those costs. Indeed, AT&T has *conceded* that the costs of “testing” – *i.e.*, of sending flesh-and-blood technicians out into the field to test a recently installed line – are *not* covered in any of its cost studies. *See* AT&T Resp. to Hrg. at 5. Instead, AT&T simply criticizes Qwest for “assum[ing]” that “Qwest will be required to send a technician to the customer premises a substantial portion of the time.” *Id*; *see also*, Transcript of January 25, 2002 Oral Argument at 45-46 (AT&T stating that the CLEC non-recurring cost model assumes that testing “can and will be done by the competitive carrier and not by Qwest.”). But that is a non-sequitur, because this “assumption” arises only when a CLEC *orders* the tariffed service called “coordinated installation *with testing*” and thereby specifically *instructs* Qwest to “send a technician to the customer premises.”

In one of its briefs, AT&T separately suggests in passing that “installation of a network interface device” should somehow be treated as a substitute for the quite different testing functions at issue here, and that the charge for the former would suffice for the latter. AT&T Resp. to Hrg. at 5. But that is nonsensical: “installation of a network interface device” is not remotely similar to “coordinated loop installation with testing.” If AT&T wants the latter service, with its carefully defined battery of sophisticated line tests, it must pay for the costs of

that service, not for the costs of some *other* service with lower costs. The ALJs may have been referring to AT&T's argument on this point when they observed that AT&T has claimed that "any testing costs incurred by Qwest, at the CLECS' request, could be recovered through a miscellaneous charge." Supp. RO&O at 8. But the ALJs do not even endorse that argument, much less identify how Qwest could ever impose or recover any such "miscellaneous charge."⁵

The ALJs discuss none of these issues; instead, they simply conclude that "the CLEC NRC model provides costs for all NRCs that are required for providing access to UNEs"; that "the CLEC model shall be adopted"; and that, by implication, a single \$1.70 charge should apply to all DS0 loop installations. See Supp. RO&O at 9. The ALJs further contend that, to avoid "anomalous results," the rate for coordinated installations (without testing) should not exceed the \$1.70 rate for non-coordinated installations, because Qwest's model reflects only a modest cost difference between the two. *Id.* As an initial matter, the modest cost difference at issue is approximately three times the amount the ALJs claim it would take to install a single loop. In any event, the ALJs' position is irrelevant, because basic loop installations themselves involve very significant labor costs. To avoid "anomalous results," therefore, the Commission should provide Qwest with true compensation for non-coordinated as well as coordinated loop installations. The Commission should also provide Qwest with substantial additional compensation for whatever labor-intensive field-testing the CLECs choose to order as well. The ALJs' proposed alternative is to pretend, at least for a while, that skilled labor costs nothing. But

⁵ AT&T and WorldCom do not contest that Qwest must recover testing costs. As noted, however, they concede that their nonrecurring cost model, adopted by the ALJs, does not include these costs. In discussions with AT&T relating to the compliance filing, it now appears that AT&T also has abandoned its claim that "miscellaneous charges" cover testing costs. Thus, it is clear that the ALJs have provided no recovery for these costs.

pretending that Qwest can hire labor for free would benefit no one, least of all the workers whose livelihood is at issue, not to mention the Arizona consumers who expect to benefit from a large and well-trained telecommunications workforce.

The result of taking these labor costs into account would approximate the rates Qwest has proposed in this proceeding: \$88.29 for a basic loop installation, \$95.38 for a hot cut without testing, and \$232.25 for a hot cut with testing. Those rates are in the same neighborhood as the rates recently adopted by the Colorado commission and the rates proposed by Staff here, and they are considerably lower than the nonrecurring costs that the New York commission recently recognized for the same loop installation functions.⁶ The Commission should thus reject the ALJs' NRC recommendations and adopt instead Qwest's proposed rates or, at a minimum, rates no lower than the Staff's original proposal of \$117.30 for basic with testing, \$58.18 coordinated with no testing, and \$141.67 coordinated with testing. *See* Qwest's Compliance Filing.

The ALJs' approach to nonrecurring costs for high capacity loops, such as DS1s and DS3s, is equally indefensible. Basic and coordinated installations of high-capacity loops require even more labor than the corresponding functions for DS0 loops. *See* Qwest Resp. to Exc. 13-14. For example, when a CLEC orders the coordinated installation of a high-capacity loop with testing, Qwest technicians, in addition to the other tasks discussed above, must design a circuit to accommodate all the locations of the relevant cables, terminal equipment, and CLEC connection points; they must often connect jumpers at the feeder distribution interface and at the customer premises itself; they must install the sophisticated terminal equipment required for DS1 or DS3 service; and they must run an array of tests to ensure an appropriately high quality of

⁶ Verizon New York Inc., Tariff PSC NY No. 10-Communications, at 47-48.

signal. *Id.* Because all of these activities impose quite significant costs, the Colorado commission recently ordered nonrecurring charges of \$154.79, \$163.84, and \$352.84 for, respectively, basic installation of a DS1 or DS3 loop, coordinated installation of such a loop without testing, and coordinated installation with testing. In contrast, under the ALJs' recommendation, the corresponding charges in Arizona would be \$23.40 *for all three* categories of non-recurring costs.⁷ Once again, the ALJs offer no explanation for how any efficient carrier could today perform these sophisticated, labor-intensive functions at such nominal levels. The Commission should reject these recommended rates and instead order Qwest's proposed rates of \$144.15 for basic, \$153.26 for coordinated no testing, and \$318.14 for coordinated with testing.

II. High-capacity loops.

Through two principal errors, relating to "fill factors" and "TIFs" respectively, the ALJs have dramatically understated the costs of high-capacity loops (DS1s and DS3s). Before addressing those errors themselves, Qwest first discusses why, when compared to the proposed rates for transport, the ALJs' proposal for high-capacity loops *must* be wrong, strictly as a logical matter.

A. High-capacity loops and transport circuits. The ALJs themselves recognized that "consistency requires adoption of the HAI model's results for both loop costs and transport."⁸

⁷ Loop provisioning is not the only area in which the ALJs' recommendation produces such anomalies. The Colorado commission recently ordered nonrecurring charges of \$55.43 and \$82.28 (depending on the circumstances) for the provision of the UNE platform over a line not currently in use (as opposed to mere "migration" of existing customers over a line already in use). Although the ALJs studiously avoid any specific reference to this issue, they appear to have recommended an untenably trivial \$0.28 charge for this function.

⁸ The ALJs recommend fine-tuning the application of the HAI model in Phase III of this proceeding to determine how best to deaverage the transport-related output of that model by

Supp. RO&O at 17. The HAI model produces transport rates – rates for a dedicated transport link between two central offices – of \$146.00 for a DS1 and \$1,749.00 for a DS3. As Qwest has previously observed, those numbers fall comfortably within the range of reasonableness established (1) by the rates in the other states within Qwest’s region and (2) by the rates set by the states in which other Bell companies have won section 271 approval. *See* Qwest Resp. to Exc. 6-7 and Exh. C. As Qwest has also previously discussed (*id.* at 3), the average cost of a DS1 or DS3 transport facility is *necessarily lower* than the average cost of high-capacity loop facility of equivalent capacity. That is because they embody greater economies of scale: unlike high-capacity loops, interoffice transport circuits are typically provided to CLECs not as self-contained physical facilities in their own right, but as channels within much larger transmission pipes. *Id.*

Thus, just as “consistency requires adoption of the HAI model’s results for both [DS0] loop costs and transport,” (Supp. RO&O at 17), so too does consistency require pricing high-capacity loops at a *higher*, not lower, level than transport facilities of the corresponding transmission capacity. But the ALJs have proposed exactly the opposite: they have recommended high-capacity loop rates of \$43.35 for a DS1 and \$516.73 for a DS3, *id.* at 4, even though those figures are roughly *two-thirds lower* than the corresponding figures for DS1 (\$146) and DS3 (\$1749) transport circuits. That makes no sense whatsoever. By contrast, Qwest’s proposed high-capacity loop rates – \$86.70 for a DS1 and \$947.85 for a DS3 – are more than reasonable when compared to the transport rates the ALJs rightly adopted.

distance. Supp. RO&O at 17. Qwest does not object to that approach, and the deaveraging issue has no bearing on the comparison discussed in the text.

B. Fill factors. In the first of its methodological errors concerning high-capacity loops, the ALJs assumed an 85% “fill factor” for these facilities. Supp. RO&O at 3 (adopting CLEC position). As Qwest has discussed, the debate about fill factors addresses the efficient utilization of capacity. Qwest Resp. to Exc. 8-10 & n.4. In adopting an 85% fill factor, the ALJs posit, in effect, that an efficient carrier would ensure that its high-capacity loops are used, on average, at 85% of their capacity at any given time. That assumption is false, because efficient decision-making often leads to low fill factors for high capacity facilities.

A simple example helps illustrate this point. Suppose that a trucking company must choose between vans and trucks as the vehicles for carrying cargo across the country. One truck has ten times the cargo capacity of a van, but the truck costs almost three times as much to operate. An economically efficient firm would substitute a truck for vans once the total cargo meets or exceeds the capacity of three vans, because the truck is less costly to send across the country than three vans. Note, however, that the total “fill” or utilization of the truck at that point is 33%. If the operator’s primary objective were simply to achieve a utilization level of 85%, he would continue to use vans until he had enough cargo (i.e., nine vans). But that would be economically irrational. At a capacity of eight vans, the operator would be spending nearly three times the amount it would cost if he had simply used the truck and “wasted” some capacity.

The same phenomenon arises in the present context as well, because the technology underlying high-capacity loops is similarly “lumpy” and “scalable.” In particular, the transmission-related electronic equipment available on the market today moves from low capacity to high capacity only in very large increments (*i.e.*, from DS1s to DS3s, with no “DS2s” in between), and the costs of those facilities does *not* increase commensurately with those increases in capacity. For example, once a carrier needs the equivalent of 10 DS1 circuits for

transport, it would cost less to purchase a single higher-capacity DS3 circuit rather than 10 separate DS1 lines, even though a DS3 can carry 28 DS1 circuits and only a fraction of that capacity would be needed to meet the carrier's immediate needs. *See generally*, Million Reb. at 31-36. Once the carrier has made that optimally efficient purchase, the resulting fill for the DS3 will be less than 40%.

This example is not the exception, but the rule, and that rule is the product of efficient practices. With any given level of demand, the facilities arrangement that *minimizes costs* often bears no resemblance to the facilities arrangement that *produces the highest fill factor*. Indeed, maximizing fill factors often produces profoundly inefficient results, such as deploying 25 DS1s to an end user rather than one DS3. And there are many circumstances in which a lower fill on a larger facility will result in lower costs, per unit and in total, and a higher fill on smaller facilities. For that reason, whether or not the ALJs are correct that the relevant "optical-digital equipment can be reinforced more easily when it is close to exhaustion" (Supp. RO&O at 3), the average efficient utilization of these facilities does not even come close to 85%. Although Qwest made this point in its exceptions-phase briefs (Qwest Resp. to Exc. 8), the ALJs simply ignored it and, as a result, overstated the fill factor for high-capacity loops. The Commission should thus adopt the more realistic fill factors in Qwest's model, which vary with the type of architecture involved and range from 37% to 100%. Ex. Qwest-18 at 28-29 (Million Reb.).

C. Total installation factors. The ALJs independently erred in adopting the radical reductions that AT&T has proposed for the "total installation factors" ("TIFs"). Those are the inputs that address the costs (among others) of warehousing equipment and transporting it to installation sites. AT&T's approach presupposes that an efficient carrier today could replace the existing network "instantaneously," Tr. at 1599 (Weiss Cross.), and that it would therefore have

no need either to warehouse any replacement facilities, *see id.*, or even to transport them from vendors to their places of installation. *See* AT&T/WorldCom Ex. 8 at 58 (Weiss Dir.). This is not our world: equipment does not magically show up where it is needed with no associated storage or transportation charges. The ALJs' approach is thus irreconcilable with TELRIC, which asks how much it would *actually cost* an efficient carrier to replace the existing network today. Pricing UNEs at any lower figure, as AT&T proposes here, would unlawfully skew the incentives of CLECs against investing in new facilities of their own. *See* Qwest Exc. 9-11.

Omitting the ALJs' erroneous adjustments concerning fill factors and TIFs would produce high capacity loop charges of \$86.70 for DS1 loops and \$947.85 for DS3s.

III. Loop-Related Inputs.

A. Terminal and Splice. One of the key inputs for the recurring loop charge is the cost of purchasing and installing a "terminal" at the end user's premises and splicing the distribution cable at that point. In the previous cost docket, this Commission "established the investment for these costs at \$70.00 per line." Supp. RO&O 1. No party introduced any evidence disputing that figure, and Staff specifically recommended that the same figure be used again.

The Recommended Order, however, adopts much lower figures – \$42.50 for buried cable and \$32.00 for aerial – on the sole ground that these are the "default values in the HAI model." *Id.* at 1-2. But the inclusion of "default values" within the CLEC-sponsored cost model is not evidence. As a result, the ALJs' recommendation for slashing the input values adopted in the prior cost docket is without any evidentiary foundation. Curiously, in all cases where *Qwest* proposed rates to which the *CLECs* did not specifically object, the ALJs withheld any recommendation and deferred consideration of the rates until Phase III. *Id.* at 18. There is no

neutral reason for taking the opposite approach – summary approval – for unsupported CLECs cost proposals that “Qwest did not specifically question” (Supp. RO&O at 2), particularly one at odds with this Commission’s own prior findings. The Commission should retain the \$70 input and defer until Phase III any additional consideration of this issue.

B. Four-wire loops. Rejecting the recommendation of Staff (*see* Staff Ex. 2), whose approach is consistent with Qwest’s, the ALJs propose setting the price for a 4-wire loop at 1.3 times the price of a 2-wire loop on the ground that “placing a four-wire loop” is not “significantly more expensive than placing a two-wire loop.” Supp. RO&O at 2. In its response to AT&T’s exceptions, Qwest explained that this logic embodies a basic statistical mistake, (Qwest Resp. to Exc. 24), but the ALJs made the mistake anyway, without acknowledging, much less responding to, Qwest’s analysis.

A 4-wire loop is the equivalent of two 2-wire loops; in effect, it is one primary line plus one second line. As Qwest and Staff agree, the price of a 4-wire loop should therefore cover the cost of two (not 1.3) 2-wire loops, minus the cost of one network interface device (which the two loops share). It is of course true, as the ALJs observe, that it costs less to place second lines than first lines. But the HAI model already takes that fact into account, *without* the ALJs’ proposed reduction, by reflecting the lower cost of placing second lines (and thus of placing the additional 2-wire pair in a 4-wire loop) in calculating the *average* cost of *all* lines. That average cost, like the associated UNE rate, applies to both primary and second lines; the HAI model does not distinguish between the two. If, as the ALJs propose, a 4-wire loop were *not* treated as equivalent to two 2-wire loops for cost purposes, the *average* cost figure for *all* lines, and thus the underlying price of a primary 2-wire line, would increase accordingly. The ALJs cannot have it both ways.

A simple example illustrates this point. Suppose that there are two customers in a cost model, and that each is served by two 2-wire loops at a cost of \$20 per customer for a total of \$40. The HAI model takes into account the cost savings that result from deploying these four 2-wire loops to only two different places: the average loop cost would be higher (say, \$70) if there were four different customers in four different places, each served by *one* 2-wire loop. Under the ALJs' approach, however, if both of the customers in the two-customer hypothetical ordered a 4-wire loop (or two 2-wire loops), the total cost of all deployed loops would arbitrarily drop from \$40 to \$26, resulting in under compensation to the incumbent of \$14. This discrepancy arises because the ALJs' proposed adjustment would double-count the cost-savings that the HAI model already takes into account *without* the adjustment.

Finally, even apart from the logical flaws in the ALJs' reasoning, there is no evidentiary basis whatsoever for the ALJs' "1.3" proposal. Indeed, no costs or assumptions in the ALJ-adopted HAI model support that proposal. *See* Qwest Resp. to Exc. 24. In sum, the Commission should reject the ALJs' recommendation on this issue and set the cost of the 4-wire loop at double the cost of the 2-wire loop, minus the cost of one network interface device.

IV. Collocation inputs.

A. Material costs. The ALJs propose slashing by 50% the material costs included within the cost model the ALJs adopted for collocation and related rates. As Qwest has explained, however, that recommendation rests on an untenable statistical fallacy. *See* Qwest Resp. to Exc. at 28-30.

The ALJs have not identified any valid basis for doubting the accuracy of the overwhelming majority of the collocation material costs that Qwest provided. Qwest's collocation cost study relies on current market rates for hundreds of different material costs. To

prove those costs, Qwest provided actual receipts from the 41 collocation jobs included in the study and verified those receipts against current contracts. Tr. at 371. The vast majority of the material costs established by these receipts and contracts were not addressed by Staff or any of the CLECs. Nevertheless, based on a recommendation from Staff that focused on the costs of termination blocks in Qwest's line sharing study, the ALJs ordered an across-the-board 50% reduction for all collocation material costs.⁹ In their attempt to support this reduction, the ALJs cite both the Staff and Mr. Lathrop's testimony relating to termination blocks.

There is no legitimate basis using a single cost for termination blocks as the justification for a 50% reduction in hundreds of other material costs in a collocation study. Indeed, the total cost of 89 terminating blocks was only about 1% of the total material purchases for the 41 collocation jobs that were studied in compiling the Qwest collocation model. Tr. at 861. The ALJs have taken testimony on this one small component of collocation and extrapolated it into a disallowance of half of all material costs in the study. That makes no sense whatsoever as a statistical or a logical matter.

The Staff and the CLECs had months¹⁰ to scour the model results and the records and could only identify a few instances in which they could even attempt to dispute the material costs

⁹ The Staff found that the costs for this terminating block had changed from costs for this item that were included in a 1997 DSL study filed with the FCC. CLEC witness Lathrop (WorldCom Ex. 13 at 59) also found fault with the purchase price of this item in his testimony and proposed an adjustment that the ALJs adopted in his initial decision.

¹⁰ The CLEC collocation witnesses have had access to the same model since September of 2000 when the company filed the study in the Washington Cost Docket, a docket in which they also testified.

Qwest included in its study.¹¹ See Supp. RO&O at 6 (citing WorldCom Ex. 13, at 59; Tr. 1131-33).¹² All parties had access to a long list of information that they could use to dispute the material costs in the models (i.e., standard price lists such as RS means and Cobra Cable and Wireless, their own contracted prices for these items, Qwest material receipts for the 41 collocation jobs, etc.).

The ALJs now propose an across-the-board 50% reduction for all material costs, apparently reasoning that an example or two is somehow representative of the accuracy of Qwest's cost study *as a whole*. That makes no sense as a statistical matter, because the examples were not chosen at random: they were singled out by Qwest's opponents in this proceeding after months of scrutinizing the record in search of as many cost discrepancies as they could find. These examples provide no logical basis whatsoever for reducing *all* of Qwest's collocation-related materials by 50%, or indeed by any significant figure at all. If anything, the other parties' very inability to identify any further cost discrepancies tends to confirm that Qwest's materials costs are quite accurate on the whole. The ALJ adopted adjustments in his first order to address the material price discrepancies identified by the other parties. No further adjustments are required.

¹¹ The CLECs also proposed an adjustment to the cost of power cabling. In the initial RO&O, the ALJs adopted this adjustment. This adjustment was not identified by the ALJs in their findings adopting the 50% adjustment. However, similar to the block costs, the actual power cable costs is only a small fraction of the total material costs of a collocation job.

¹² Although the ALJs cite a passage (Tr. at 804-07) discussing a supposedly inflated cost for "flat washers," Qwest clarified that it paid a market rate of \$0.98 for *a bag of 100 washers*, not for each individual washer, as Staff has absurdly suggested. See Tr. at 879-80 (Fleming Cross.); Qwest Resp. to Exc. 28. The ALJs do not find otherwise.

B. Power cable lengths. It is undisputed that, under the conditions actually found in an exhaustive study of collocation arrangements in Arizona central offices, the average length for a specialized *DC* power cable can be either 70-80 feet or 177 feet. Which of those figures is applicable depends on a given CLEC's need for *DC* power -- in particular, on whether that need is great enough to justify bypassing the intermediate power board and running a power cable directly from the CLEC's collocation space all the way to the main power board. *See* Qwest Resp. to Exc. 25-26. Where the need does reach that level, it is undisputed that the average length of this longer power cable in actual Arizona central offices is approximately 177 feet.

The ALJs, however, propose treating the latter 177-foot cable as though it were a 70-foot cable on two grounds, each of which is unsound. First, the ALJs claim that using only the 70-foot figure, even when CLECs order 177-foot cables, is "consistent with Qwest's own space rent study which includes a standard length for cabling for a typical central office." Supp. RO&O at 7-8. Here the ALJs have simply confused *AC* power cords with *DC* power cords. The space rent study addresses a CLEC's need for a standard *AC* power cord for general power needs, not the more specialized *DC* power cords at issue here, which are required for specialized telecommunications purposes. *See* Tr. at 426-428; WorldCom Exh. 6. Because the space rent study does not address the need for a standard *DC* power cord, it is inappropriate to use it as a basis for the finding. Second, the ALJs claim that pretending that a 177-foot cable is actually only 70 feet long is "consistent with the observance of a forward-looking network that includes modern central offices requiring shorter cable lengths." Supp. RO&O at 8. But the ALJs cite no evidence for this conclusion, and indeed none appears in the record.

C. Market-Based Pricing.

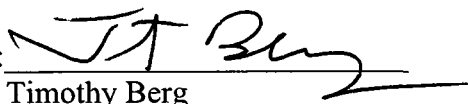
At Supp. RO&O 13-14, the ALJs deny Qwest's request for market-based rates for certain information services and data base elements. The ALJs propose that, if Qwest wishes to have flexible rates set for these services, "it should submit appropriate tariff filings pursuant to the Commission's rules and Decision N. 63487." Supp. RO&O at 14. The issues of the extent of the Commission's jurisdiction over the prices for these services and the appropriate level of such prices should be deferred to Phase 3 of this Docket.

CONCLUSION

Based on the foregoing arguments and those in Qwest's other submissions, the Commission should grant Qwest's exceptions to the RO&O and Supplemental RO&O and make the changes to the ALJs' recommendation as referenced in the discussion above, in Qwest's response to other parties exceptions, and in Qwest's original exceptions (and the reply in support thereof).

Respectfully submitted this 21st day of March, 2002.

By:


Timothy Berg
Theresa Dwyer
FENNEMORE CRAIG, P.C.
3003 North Central, Suite 2600
Phoenix, Arizona 85012-2913
(602) 916-5421
(602) 916-5999 (fax)

Roy Hoffinger
Wendy Moser
QWEST CORPORATION

John M. Devaney
Norton Cutler
PERKINS COIE LLP
Attorneys for Qwest Corporation

ORIGINAL and 10 copies of the
foregoing hand-delivered for
filing this 21st day of March, 2002
to:

Docket Control
ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, Arizona 85007

COPY of the foregoing hand-delivered
this 21st day of March, 2002, to:

Commissioner William A. Mundell
ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, Arizona 85007

Commissioner Jim Irvin
ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, Arizona 85007

Commissioner Marc Spitzer
ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, Arizona 85007

Maureen Scott
ARIZONA CORPORATION COMMISSION
Legal Division
1200 West Washington
Phoenix, Arizona 85007

Ernest Johnson
Director, Utilities Division
ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, Arizona 85007

Lyn Farmer, Chief Administrative Law Judge
Hearing Division
ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, AZ 85007

COPY of the foregoing e-mailed and
sent by regular mailed this 21st day of
March, 2002, to:

Steven J. Duffy
RIDGE & ISAACSON, P.C.
3101 North Central Avenue, Ste. 1090
Phoenix, Arizona 85012-2638

Richard S. Wolters
M. Singer-Nelson
AT&T
1875 Lawrence Street, Room 1575
Denver, CO 80202-1847

Allen Wong
AT&T
1875 Lawrence Street, Room 1575
Denver, CO 80202-1847

Michael W. Patten
ROSHKA HEYMAN & DEWULF
400 North Fifth St., Ste. 1000
Phoenix, AZ 85004-3906

Michael Grant
Todd C. Wiley
GALLAGHER & KENNEDY
2575 E. Camelback Rd.
Phoenix, AZ 85016-9225

Thomas H. Campbell
LEWIS & ROCA
40 N. Central Avenue
Phoenix, AZ 85007

Brian S. Thomas
TIME WARNER TELECOM
520 SW Sixth Ave., Suite 300
Portland, OR 97204-1522

Thomas F. Dixon
WORLD COM
707 17th Street
Denver, CO 80202

Eric S. Heath
SPRINT COMMUNICATIONS CO.
100 Spear Street, Suite 930
San Francisco, CA 94105

Scott S. Wakefield
RUCO
2828 N. Central Avenue, Suite 1200
Phoenix, AZ 85004

Ray Heyman
ROSHKA HEYMAN & DeWULF
400 North 5th Street, Suite 1000
Phoenix, AZ 85004

Rex M. Knowles
XO Communications, Inc.
111 E. Broadway, Suite 1000
Salt Lake City, UT 84111

Megan Doberneck
COVAD COMMUNICATIONS COMPANY
7901 Lowry Boulevard
Denver, Colorado 80230

Lisa Crowley
COVAD COMMUNICATIONS COMPANY
4250 Burton Drive
Santa Clara, CA 95054

Greg Kopta
DAVIS WRIGHT TREMAINE LLP
2600 Century Square
1501 Fourth Avenue
Seattle, WA 98101-1688

Mary S. Steele
DAVIS WRIGHT TREMAINE, LLP
2600 Century Square
1501 Fourth Avenue
Seattle, WA 98101-1688

Dennis Ahlers
Senior Attorney
ESCHELON TELECOM, INC.
730 Second Avenue South, Suite 1200
Minneapolis, MN 55402

Steve Sager, Esq.
MCLEODUSA TELECOMMUNICATIONS SERVICE, INC.
215 South State Street, 10th Floor
Salt Lake City, Utah 84111

Marti Allbright, Esq., Esq.
MPOWER COMMUNICATIONS CORPORATION
5711 South Benton Circle
Littleton, CO 80123

Penny Bewick
NEW EDGE NETWORKS
PO Box 5159
3000 Columbia House Blvd.
Vancouver, Washington 98668

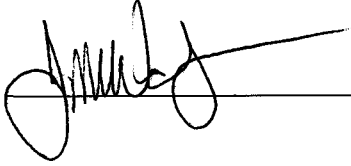
Michael B. Hazzard
KELLEY DRYE AND WARREN
1200 19th Street, NW
Washington, DC 20036

Janet Livengood
Z-TEL COMMUNICATIONS, INC.
601 South Harbour Island
Suite 220
Tampa, Florida 33602

Andrea Harris
ALLEGIANCE TELECOM
2101 Webster
Suite 1580
Oakland, CA 94612

Traci Grundon
DAVIS, WRIGHT TREMAINE, LLP
1300 S. W. Fifth Avenue
Portland, OR 97201

Joan Burke
OSBORN MALEDON
2929 N. Central Avenue
Phoenix, AZ 85012



PHX/1283310.2/67817.240

BEFORE THE ARIZONA CORPORATION COMMISSION

WILLIAM A. MUNDELL

Chairman

JIM IRVIN

Commissioner

MARC SPITZER

Commissioner

IN THE MATTER OF THE GENERIC)	
INVESTIGATION INTO U S WEST)	
COMMUNICATIONS, INC.'S COMPLIANCE)	DOCKET NO. T-00000A-00-0194
WITH CERTAIN WHOLESALE PRICING)	PHASE II
REQUIREMENTS FOR UNBUNDLED)	
NETWORK ELEMENTS AND RESALE)	
DISCOUNTS.)	
)	

STATEMENT BY HARRY M. SHOOSHAN III

March 21, 2002

My name is Harry M. Shooshan III. I am president and co-founder of Strategic Policy Research, Inc. ("SPR"), a communications policy consulting firm located in Bethesda, Maryland. Prior to founding SPR, I worked for eleven years on Capitol Hill and, for six years, was Chief Counsel and Staff Director of the Communications Subcommittee in the U.S. House of Representatives. I was an adjunct professor at Georgetown University Law Center from 1976 to 1991, teaching communications law and regulation. In my twenty-one years as a consultant, I have advised a wide range of clients in the private sector as well as governments and regulatory bodies in the United States and around the world. I have testified before numerous state public utility commissions, including this Commission as a consultant to the Staff, on issues relating to

structural separation, competition, customer perspectives on telecommunications markets, price caps and other forms of incentive regulation.

Last month marked the sixth anniversary of the Telecommunications Act of 1996 ("TA96"). Although TA96 appointed the Federal Communications Commission ("FCC") the "federal captain" of the "team," many of the difficult decisions reside with the state public utility commissions ("PUCs" or "commissions"). The state commissions have had to face difficult decisions that require balancing a variety of interests and equities. The FCC has set the policy and pricing standards but the implementation of these policies and pricing principles by state commissions will ultimately determine the success of competition within a state. And it is the implementation of the FCC pricing guidelines that will ultimately decide whether customers experience the benefits of thriving facilities-based competition.

In implementing TA96, the FCC adopted a cost model that is designed to establish prices for "Unbundled Network Elements" ("UNEs") at levels that reflect a forward-looking environment. The FCC model embodies "scorched earth" engineering assumptions. By this I mean that the model had as its baseline an assumption that the network being unbundled is built from scratch with the latest technology in the most-efficient architecture for current market conditions. The results depend, among other things, on assumptions about:

- Equipment costs, which are never divulged by the manufacturers, and which vary enormously according to the overall relationship between the vendor and the customer;
- Fill factors, particularly in the loop plant, that can swing the cost estimates by factors of two or three;
- Operating efficiency, including labor productivity and OSS costs;
- Financial conditions, including debt ratios and required returns; and
- Growth rates of various services.

Each of these parameters, as well as a number of others, obviously cannot be determined with any precision. Indeed, in proceeding after proceeding, ILEC experts and CLEC experts present detailed “studies” of the costs, which often differ by factors of two or three.

The record in this proceeding is replete with arguments from all parties, including the staff, about what the appropriate assumptions should be. I do not intend to enter that fray. It is important, however, that the Commission keep in mind that the starting point for the debate over UNE prices is to determine what it would cost an efficient carrier to replace and operate the network *today* using the most efficient technology that is currently available. I agree with Qwest that the ALJ’s decision would produce UNE rates for Arizona that fall sharply below even what TELRIC requires. The result would be an exceptionally unfortunate blow to long-term consumer and competitive interests in this state. If not implemented carefully, TELRIC will tip the scale heavily against facilities-based competition.

On another front, the FCC has been aggressive in reducing interstate access charges.¹ Lowering intrastate access charges—while desirable in the context of rationalizing prices—presents problems for state commissions because it also entails rate rebalancing and replacing the contribution that carrier access services provide to covering the total costs of the incumbent. The decisions the FCC and this Commission have made regarding access charges are important in this Docket because UNEs (especially UNE-Ps) provide long distance carriers with a cheaper alternative to carrier access.

Regulators, especially on the state level, have had to make some tough calls with regard to both wholesale (competitive inputs) and retail prices in the aftermath of TA96. State commissions have had to make a series of interrelated decisions that are analogous to calibrating a number of dials. If you turn the dials too far one way, you foreclose important competitive

¹ Under the CALLS Plan adopted by the FCC, interstate switched access rates were reduced to \$0.0055 per minute as of January 2002. This reduction in interstate rates has put additional pressure on state commissions to lower corresponding intrastate access rates.

opportunities (and harm consumers). But if you turn them too far the other way, you harm the incumbent and undercut the incentives of *all* players to invest in telecommunications networks (which also harm consumers).

In fact, just last year, the ACC had to balance a number of competing interests in adopting the price regulation plan for Qwest. The price cap plan seeks to protect consumers by imposing a "hard cap" on prices for flat rate local exchange services, while implementing reductions in intrastate access charges that will benefit long distance carriers and, presumably, lead to lower long distance prices in Arizona. In order to be fair to Qwest, the company was given additional upward flexibility ("headroom") in pricing competitive services in Basket 3, corresponding directly to the access charge reductions. As I testified at the time, local competitors benefit from having all of the inputs they purchase from Qwest (UNEs and resold services) placed in a separate basket governed by their own pricing rules. However, should UNE rates be reduced from their current levels, I believe that Qwest must be given additional flexibility in the price regulation plan in order to maintain the balance that was struck. Perhaps, the Commission might reconsider the "hard cap" on basic local exchange services (and/or some of the caps on individual rate elements) or slow down the pace of access charge reductions to permit Qwest the opportunity to "make up the difference." My own preference would be that you not drive UNE prices down to levels where it would be necessary to reopen what I believe is a very progressive price regulation plan.

Ultimately, however, the ACC should adopt policies in proceedings such as this to promote facilities-based competition, or at least not discourage it, consistent with your obligations under the Arizona Constitution and statutes and TA96. The ACC's objective should be to create the conditions for a self-policing competitive marketplace. The FCC recognizes this. As Chairman Powell has said:

Facilities-based competition is the ultimate objective. I believe that other methods of entry are useful interim steps to competing for local service, but

Commission policy should provide incentives for competitors to ultimately offer more of their own facilities.²

Surely, the “interim” period must have an endpoint if we want to achieve what Chairman Powell call the “ultimate objective.”

It is important for this Commission to understand the tradeoffs and their implications. For the past six years much of the emphasis in regulation has been placed on “service competition” rather than “network competition.” By “service competition” I mean competition among providers of what is essentially the same service since it relies on the underlying facilities of the ILEC. On the other hand, I use the term “network competition” to refer to the type of competition that involves competitors’ use of their own facilities (e.g., Cox Communications in Arizona).

The argument in favor of setting “low” unbundled network element (“UNE”) prices is to make it cheaper for CLECs to “buy” (that is, to rely on the incumbent’s network) rather than to “build.” The superficial attraction of setting UNE rates below costs is to show quick results (i.e., lots of competitors) to the “success” of TA96.

This can also be seen as a means of putting additional downward pressure on access charges—both interstate and intrastate. For example, the UNE-platform (or UNE-P) provides a lower-priced alternative for carrier access; both perform essentially the same function when purchased by a competitor that happens to provide long distance as well as local service. These policies favoring service competition, coupled with inefficient retail prices, have created arbitrage opportunities that have been central to the business plans of most CLECs, many of which are failing as these opportunities disappear along with the high-risk venture capital of the late 1990’s that fueled their rapid growth.

² FCC Chairman Michael Powell, “Digital Broadband Migration,” Part II (October 23, 2001).

It is not surprising to see competition develop as it has. Today, there are many facilities-based options for larger business customers and even higher-usage residence customers, but far fewer, if any options, for the average residence customers. AT&T, for example, is focusing its effort on what it calls "high-value" customer. According to AT&T's Consumer Division president and CEO, "(g)reater than 70 percent of our [profits] comes from about 25 percent of our customers, and so we are keenly focused on them."³ Another major competitor, Cox Communications, provides integrated packages of cable television, local and long distance services, and Internet access to residences in limited areas of North Phoenix, Scottsdale, Peoria, Tempe and Mesa.⁴ Cox has indicated that it may extend telephone service to its Tucson cable service area by late 2002, after some pilot testing.⁵

Among the factors limiting competition for residence customers is that, to delay Bell company entry under Section 271 of the TA96, large interexchange companies ("IXCs") have strategically chosen not to mass market-local telephone service. By asserting that local competition is being thwarted, AT&T and WorldCom seek to gain additional concessions from the BOCs and more favorable treatment by regulators, while at the same time arguing that "conditions are not right" for the price-reducing benefits of BOC entry into the long distance market. The irony is that, as the FCC and others have observed, local competition is the most intense in states where interLATA relief has been granted and the IXCs no longer have anything to gain from delay.⁶

³ Betsy Bernard, AT&T Consumer President and Chief Executive Officer, speech before Salomon Smith Barney Entertainment, Media, and Telecommunications Conference (January 7, 2002) 6-7, 12.

⁴ <http://www.cox.com/Phoenix/telephone/FAQ's.asp>. (visited February 8, 2002).

⁵ "Tucson Ariz. To See First Stage of Telephone Service Competition," *The Arizona Daily Star* (August 29, 2001).

⁶ See "Local Telephone Competition: Status as of December 31, 2000" (May 2001). See also J.A. Hausman, G.K. Leonard and J.G. Sidak, *The Consumer-Welfare Benefits from Bell Company Entry into Long-Distance Telecommunications: Empirical Evidence from New York and Texas* (January 9, 2002).

While I firmly believe that competition among networks provides greater long-run public benefit, I do not diminish the role of service competition. It is real competition; that is, a competitor using UNEs or resold lines from Qwest can “capture” the customer and all of his/her usage, including vertical features, toll usage, and Internet access.

But service competition is only part of the picture. A car analogy will help to illustrate this point. While hood ornaments, trim, brand name and price are the differentiating features between, say a Cadillac and a Chevy, these vehicles compete to satisfy a range of consumer choices depending on their preferences. The interesting point is that, while the outside packaging is different, under the hood, they are essentially the same car—both built by General Motors.

With service (as opposed to network) competition, the similarities among competing retail products are even greater. Local telephone service providers are reselling or “reprovisioning” precisely the same service or loop that the incumbent provides; it is simply being rebranded or repackaged. You may recall that one of the early disputes following TA96, was whether ILEC installers had to wear AT&T patches on their uniforms when servicing retail customers of AT&T served by the ILEC network.⁷

While there are opportunities for innovation, even by resellers, these opportunities are more typically associated with pricing, billing and packaging. True innovation is not possible because the underlying network remains the same. In the automobile industry, real competition and choice—and efficiency—were injected into the market by the entry of fuel-efficient and otherwise advanced automobiles from foreign manufacturers (principally the Japanese) in the late 1970s. Similarly, the deployment of competing networks will provide choices for consumers that are simply not possible with resellers and UNE-based competitors.

⁷“Phone War Rivals Slug it Out,” *The Omaha World-Herald* (July 22, 1996) at 13.

Network competition offers the real prospect for new investment, innovation and customer choice. Only network competition will, in time, enable this Commission to remove itself from regulating the prices for both retail and wholesale services. While use of ILEC services and network elements in general will still be an option for the foreseeable future, resale and UNE rates should not be set so as to favor reliance on the ILEC network over self-policing facilities-based competition.

My role here is not to offer support for either of the cost models used in this proceeding or to engage in a detailed critique of the ALJ's recommended order. I would like, however, to cast the issues in this proceeding in terms of the larger picture of the telecommunications markets and the overall policy objectives of this Commission.

As a commission, you have discretion in this proceeding. But the zone of reasonableness in setting UNE prices is not boundless. Admittedly, there may be differences as to what should constitute the bounds of that range. For example, while \$25.95 (Qwest's proposed statewide average) may be too high, \$12.62 (the ALJ's proposed statewide average) is difficult to defend under any circumstances.⁸ In my opinion, it is more damaging to long-run consumer welfare and to efficient competition to set UNE rates too low as to set them too high.

I would like to suggest that you step back from the complexities of cost models and consider the larger objective of providing for competitive telecommunications in Arizona. I do not presume to tell you where the right point in the zone of reasonableness should be, but rather to ask you to consider the consequences of where you do, in fact, come out in your decision. To put things simply: if UNE prices are set too low, you undercut the incentives for new entrants to build or “redeploy” (as is the case with cable network upgrades) facilities and networks in

⁸ The complexity of the decision in this proceeding is illustrated by the fact that parties take different views of the ALJ's proposed treatment of cost components and their impact on the proposed UNE cost. AT&T estimates that the ALJ's recommended treatment of cost components would result in a UNE loop rate of \$12.13, while Qwest estimates that the ALJ's recommendations yield a UNE loop rate of \$14.54.

Arizona. There is no need for firms to deploy expensive networks in Arizona if the UNE prices (and wholesale discounts) are extremely advantageous. Setting UNE prices too low will also undercut the incentives for Qwest to invest in Arizona since it knows that its capital is "at risk." The combination of the policies of low UNE prices and low retail prices for, say, residential service (which are "hard capped" for three years under your price regulation plan), makes it even more difficult for facilities-based competition to develop for those customers. My chief concern about the ALJ's draft order in its current form is that, as I read it, the recommended UNE loop rate was calculated precisely to come out just below the already low IFR rate.

In my opinion, network competition will continue to expand if regulators resist the temptation to turn the regulatory dials too far in the direction of promoting service competition. Three major types of alternative network technologies are already in place and competing with ILEC networks, including Qwest's in Arizona. This is what the AT&T has called "technology substitution."⁹ Mobile wireless networks are already carrying calls that a few years ago would have been carried over wireline networks.¹⁰ Further, for some customers, mobile phones already have replaced wireline phones (e.g., for second lines). Wireless operators such as VoiceStream and Leap Wireless are marketing their products as direct substitutes for residential wireline service. Leap's Cricket service has been "designed for people who primarily want local calling

⁹ Bernard at 14. *Op. cit.* In addition to wireless, Ms. Bernard points to the Internet (email) and instant messaging as competing with the voice platform.

¹⁰ SPR conducted surveys of business customers in New Jersey and (residence customers) in Illinois that found that a significant portion of customers were making calls on their wireless phones that they might otherwise have made over their wireline phone at home or at the office. See Harry M. Shooshan, Testimony on behalf of Bell Atlantic-New Jersey before the Board of Public Utilities ("BPU") in New Jersey, BPU Docket No. TO99120934 (May 17, 2000); Panel Testimony of Harry M. Shooshan, William E. Taylor, and Joseph H. Weber on behalf of Verizon New Jersey before the BPU, BPU Docket No. To020095 (February 15, 2001); and Harry M. Shooshan, Testimony on behalf of Ameritech Illinois before the Illinois Commerce Commission, Docket No. 98-0860 (Ameritech Illinois Ex. 5.0, March 12, 1999).

service for a fee similar to their wireline service.”¹¹ Additionally, cable networks are being reconfigured to handle voice, data and Internet access. Households with cable modem service typically drop—or do not add—second phone lines. Finally, satellite communications networks should not be ruled out as major alternatives to ILEC networks. Satellite networks are used to transmit data for multi-location business. Their use in voice communications and for providing services to residence customers (e.g., broadband Internet access) is increasing. Satellite networks may be especially important for providing high-quality, affordable service in rural areas.

There are many dimensions to your decision in this case. You will not be acting in a vacuum. Consider the implications of what you do here for the very progressive price cap plan you adopted last year. Under that plan, Qwest has agreed not to increase its 1FR rates for three years. In fact, in real terms, those rates could actually decline under the price cap formula. That plan also placed “wholesale services” such as UNEs in a separate basket with prices to be determined by proceedings such as this. UNE rates must be set based on costs; if those rates are set below costs you may jeopardize the balance that was struck in the price cap plan and the benefits to consumers that are a key part of that plan. This is yet another reason to reject the ALJ’s extreme pricing recommendations.

In the end, what is required of you is a careful balancing of the legitimate needs of competitors and the incumbent, of shareholders and ratepayers, consistent with the standards that

¹¹ “Leaping Ahead And Taking A 3G ‘Slice,’” *Wireless Week* (March 11, 2002) at 37. Leap Wireless reports that about 7 percent of its customers no longer use wireline connections and 61 percent use their cell phone as their primary phone. [Yuki Noguchi, “More Cell-Phone Users Cut Ties to Traditional Service,” *Washington Post* (December 28, 2001) from www.washtech.com.] In November 2001, the Cellular Telecommunications & Internet Association’s (CTIA) Wireless Foundation, in cooperation with Nokia and Cellular One, donated 30,000 wireless phones to support the “Vision One” program in Arizona and New Mexico. This program, developed in consultation with the Arizona Corporation Commission, helps provide Native Americans with reduced-cost access to wireless phone service which is described in the CTIA’s news release as “an alternative to wireline communications...and [becoming] the primary means of communications, reaching past the limitations of wireline networks.” See CTIA News Release (November 19, 2001) at www.wow-com.com/articles.cfm?ID=647&SearchSection=&SearchCriteria=arizona.

have been set for you. It comes down to your collective judgment about what is reasonable. I am confident from having seen this Commission work through difficult issues in the past that you will "do the right thing."